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# SOC. ALEXANDER RODRIGUES LTD.:

# WHEN MINORITY HOLDS THE POWER

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# ABSTRACT

This case presents a real decision set regarding the future of a family business reaching its 6th generation, whose high dispersion of shares and estrangement between family branches yielded a risky deadlock for the business growth and survival. Written from the family CEO's perspective, the case depicts his need to attract the passive and dissenting wings of shareholders, after running through the whole history of relational problems between them. At stake is a nonconsensual diversifying investment opportunity, which is key to the survival and growth of the business, yet is dependent on a hardly attainable qualified majority voting. [*]

*Keywords:* Family Business, Ownership Conflict, Socioemotional Wealth, Fair Process

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Inês Vaz Pinto and the referred Company, who welcomed me with open arms;

God, who loves me, dwells me and sustains me every day.

[*] All names, dates, locations, and exact values have been disguised. Nonetheless, when relevant for the analysis, their relative proportions were preserved.

# WHEN MINORITY HOLDS THE POWER

The spring of 2015 had showed up with the warmth of the morning sun and a gentle breeze in the air, so Leonardo took the opportunity to sit down watching the river flow. This daily half-hour walk to the office was the best moment to clear his mind and he was in no rush: by then, his son Nicolas, who was already in charge of most of the productive and commercial duties, had for sure reached the facilities in the riverside of Lisbon. He trusted his firstborn was faster and more competent in his job than himself, which combined with the unique conditions of the family farm should offer him plenty reasons to be optimistic about the future, and yet, he just could not rest easy on that.

His main concern was not to manage the business, but rather how to manage his own family: with 104 shareholders spread between the $4^{th}$ and $6^{th}$ generations, a constantly growing number which would soon grow to more than 200, wrangling was increasingly threatening continuity. The company urgently needed to find a new governance structure, to cope with these challenges and to simultaneously enable the launch of a major expansion.

Until the night before, Leonardo was determined to convene a general meeting for the following month, where the Board would try to push through an amendment of the articles of incorporation. However, having read a couple of the latest emails that some cousins often sent to the whole family, contesting and spreading the fear about his intentions, the CEO had to admit the current chances of such approval were minimal but still had no clue what else he could do to convince them.

“This may well be the last chance for the family to function as such before it becomes an unmanageable group of strangers.” – He thought, whilst watching a meticulously choreographed crew sailing some vessel in the river – “We cannot put our interests ahead of the company, we only have it borrowed from our children and we owe them a sustainable future! How can they ignore such responsibility?”

# Soc. Alexander Rodrigues Ltd.

## Building a legacy, Rodrigues by Rodrigues

**Alexander** – It was the spring of 1875, precisely 140 years before, when Leonardo's great grandfather arrived to Quixote, a small village in the remote countryside of Portugal, sitting in a horse-drawn chariot. Despite being thought to be deluded for buying such inhospitable terrains, Alexander Rodrigues had a visionary belief in the profitability of the cork business to the point of investing everything he had in the purchase of the oak forests he had heard that existed in that region. More than 2000 deeds later, he had gathered a 5500 hectares estate, including smaller plots of vineyard and olive groves. Additionally, the entrepreneur created a pioneering industrialized factory of cork stoppers on site and made every effort to link the underdeveloped region to Lisbon through railway. This latter achievement allowed him to carry the production outputs to the still-in-use headquarters in Lisbon, in a 16$^{th}$ century building he had acquired and adapted to an administrative and warehouse facility, before exporting them worldwide. Later, in 1902, Alexander established the business as the first agricultural private limited company (Ltd.) in the country, whose articles of incorporation obliged to keep ownership within his direct offspring in order to assure continuity across generations. By the time of his death, he left it to his nine living heirs, including his second wife, as shown in Appendix 1.

**Gabriel** – The articles also set that the board should have three directors but only one fully executive, while others held more advisory roles. Gabriel was the chosen one to continue pursuing the founder's dream, cause for which he devoted more than thirty years, taking the effort to streamline, monetize and expand the three productions. Back then, he used to move in with his family to the farmhouse for a couple of months during the warm season. His half-brother Ignacio, with whom he kept a strong relationship, would often come along and grew close to his same age nephew Paul, becoming as inseparable ‘brothers’. Meanwhile, as Gabriel aged, the former began to become more and more involved in the business, helping him, while the latter preferred to devote himself to a promising career as a lawyer in the capital. Therefore, when the time came to find a successor upon his death, the choice had consensually fallen over Ignacio, with Paul claiming he would rather occupy only one of the consultative Board seats together with a son of his aunt Fatima.

**Ignacio** – the founder’s youngest son is now proudly remembered for having a selfless heart which, with his roots deeply embedded in Quixote, led him to dedicate most of his life and mandate to the local development. Nevertheless, it has not always been like this: for a good part of his term, Ignacio faced open contestation from some of his nephews.

At first, strife appeared when he requested the family’s approval to issue a considerable amount of debt to invest on the construction of two dams. The region was particularly arid and the brook that crossed the property dried every summer, often leading to wipeouts of the wine and olive crops that could otherwise be avoided through water retention. Therefore, when the Portuguese government, embedded in the 60’s boom spirit, issued a credit line with extremely favorable conditions to promote such investments, Ignacio did not want to let the opportunity slip away. Yet, he had a hard time convincing some relatives who feared that if something went wrong they could see their personal assets pawned, even though this was not legally a possibility in private limited companies. Then again, when he started his philanthropic mission, which included the building and furnishing of dozens of homes and public facilities for the local community, his family complained he could not spend the company’s resources in such way. The administrator even had to present invoices proving everything had been paid from his own pocket.

In light of the repeated criticism, Ignacio quitted general assembles for more than once, claiming he could not stand it anymore. In any case, the family always immediately and unanimously voted for his continuity. The leader’s incredible aptitude for advocacy of the region was granting a lot of support to the cause, even from the highest spheres of society and government, and therefore, by the end of his life, the entire family was proud of the reputation built towards their name. Indeed, even nowadays most of the farm workers live in houses lent by the company to which they dedicate their whole life.

**Alexander II** – In 1972, the third Board taking control of the company was composed by three children of the previous administrators, but the economic and social circumstances found were quite the contrary. Shortly after their election, Portugal had undergone the 1974 revolution that placed all agricultural businesses under threat by land reform. The family managed to avoid the farm's expropriation but still suffered serious implications, mostly due to the absolute lack of outlet for that year's production. Moreover, unlike hitherto, agriculture companies had to start paying VAT, employee's social security and corporate taxes. With the company under severe financial stress, Alexander requested the shareholder assembly for capital injection, but the will of some relatives was far the opposite: given all the uncertainties, they would rather liquidate assets and cash in as much as possible. Such divergence brought heated debate during the following years, but neither sides were able to gather the required 75% of the shares support. Anyhow, the firm managed to survive thanks to its entry in the fruit farming business, made possible by the implementation of an irrigation system from the dams concluded in the meantime. Despite this culture being considerably profitable for a couple decades, after which it was replaced for more vineyards, the firm still needed a large expenditure retrenchment.

**Leonardo** – The current CEO took the seat, accompanied by two cousins from David's and Fatima's branches, keen on recovering the firm from the consequences of the downturn. Indeed, the strengthened economic confidence in the 90's, along with cork's prices going out off the roof, allowed the company to significantly invest in a needed modernization of processes, machinery and facilities, but not for long.

### “So, how’s the business?”

**Olive Oil –** This was the first culture to be revamped, with the construction of a state-of-the-art mill, the product’s premium rebranding and organic certification, and constant presence in international fairs and contests. The resulting quality had no match in the market and granted plenty awards and publicity.  However, besides the increased competition in the premium market pulling down margins since then, the financial impact of this culture is residual due to its small acreage (120 hectares). As a result of both factors, the firm favors sale to small loyal retailers without intermediaries.

**Wine** – Wine-making has gone through the exact same process as olive oil but only more recently, because it first involved having the already too aged 26 hectares of vineyards gradually replanted over the last 20 years. Wine had been mostly sold in bulk to the same company for decades, which granted safe but continuously declining income and low margins. Therefore, as replanting massively increased quantity and quality, Leonardo hired his son Nicolas - upon family’s approval – to help him gather and lead a new team responsible for creating and marketing the organic and biodynamic product under new own labels. Once again, the firm’s strategy was paying off but had limited capacity: each year a larger portion of the harvest was kept for the own brand, and then exported worldwide.

**Cork** – After the 90’s, the traditional cash cow of the company became a mere shadow of yesteryear. Droughts and arsons have been decimating the population of oak for decades and all the management’s attempts of seeding did not yield any results. As shown in the Appendix 2, not only the average harvest decreased 50% in quantity over the last 40 years but also market prices have been falling continuously on the whole industry recently, causing a dramatic revenue shortfall. Unfortunately, this type of soil, that occupies 97% of the estate, is not suitable for any other cultivation.

**Overview** – Complementarily, Soc. Alexander Rodrigues owned a store and a renowned restaurant in the Quixote village, which provided residual or no profitability but were substantial in terms of publicity and reputation of the brand, family and region. Also, the ancient building in Lisbon's riverside, where the headquarters occupies only a small part, used to provide some additional income in rents, but its degradation and the prospects of a future investment have been leading to the reduction of these contracts.

Leonardo, despite the hiring of more qualified professionals, was able to significantly cut spendings but the severe shortfall in revenues – check Appendix 3 for more details - has been causing consecutive net losses over the last 4 years. Traditionally, the firm kept a zero debt policy and some liquidity that served as cushion, but it would not last much longer and there was a growing dissatisfaction amongst shareholders.

## Troubles in their own backyard

### A break in the weather

For two decades after Leonardo's election, the strife that had chased his two predecessors seemed to be gone, and general assemblies, which lasted for no more than a few hours, were peaceful conversations in his office between the Board, his siblings, and three or four more cousins. The business was going well, allowing for some historically rare dividend distribution, and despite the majority of the owners not following the reality of the company, he was still hearing some compliments from all over the family, including the traditionally disagreeing branch of Gabriel's descendants. Nonetheless, quietness was suddenly shattered again when in 2008 a group of four siblings (5% of shares) from that branch, self-titled as "dissenters", unexpectedly came for the first time to an assembly to protest against the Board's acting. The trigger had been a public warning in the newspapers announcing a lien on the company's property in Lisbon. The firm had been facing a public prosecution for a long time and, despite innocence being proven, procedural flaws made it still be sentenced to pay a fine circa its annual expenditure on wages.

## Pandora's Box

This group of dissenters then started sending emails and organizing undercover discussion meetings in Braga (their hometown, 350km from Lisbon) between some specifically chosen shareholders, in particular those less familiar and active in the business. In them, intimidated by the possibility of patrimonial losses, they casted doubts about the Board's intentions and capacities to run the company, claiming it was taking advantage of the rest of the family. As the fear spread, around 15% of passive owners granted to be represented by the dissenters, while others remained supporters of the Board or barely reacted, but very few from either side actually sought any clarification directly from the management.

Thereafter, never were assemblies the same. Despite the increased percentage of capital present (Appendix 4), it did not translate into much more attendees, as most of the shareholders always preferred to appoint a relative as their proxy holder. The atmosphere, however, was now invariably tense, with some heated accusations occasionally erupting from the middle of the dissenters' lengthy dictations of highly technical questions to the minutes. These entailed great difficulty and time for the Board to answer, and the replies seemed to barely interest even the own arguer. As a result, the few supporters who regularly attended lamented there was little room for plain talk and effective enlightenments.

Leonardo was conscious of the uselessness of all this process for both sides, but still did not know how to fix it. Neither was he able to give cousins a proper insight about the business, nor could he know their will to its future. And it got even worse regarding the younger generations, since, apart from one or two exceptions as his own children, the shares were integrally held by the oldest relatives in each branch.

Although most of the interventions regarded divergences over juridical and accounting details, there was more to the matter. For instance, one of the most frequent demands was for the right to unrestricted usage of the farmhouse for family vacations.

This residence was aimed to host the management in its weekly visits to the farm, and for logistical and financial reasons, each shareholder's usage was limited to three free days per year. Since this demand kept recurring, Leonardo invited an ad hoc committee, composed by an ancient from each branch, to design a sustainable usage policy. They set a daily rate per guest that allowed to drop the time restrictions, and even though few cousins ever made use of it in the meantime, it was enough to stop those specific complaints.

For another thing, from time to time the dissenters shot the breeze about the lack of dividends, but turnover was so small compared to the dispersal of shares that the management and its supporters preferred to keep the business healthy rather than drain its wealth. It was thanks to the consecutive retained earnings that the company had been able to do all the revamping processes without debt. In fact, the last time the business had had considerable gains, the Board had even opted to offer a supplementary wage to all employees in that year, instead of distributing dividends. "They are our most valuable asset! Even the new ones take up the cudgels for the company as most cousins would never" – considered Leonardo.

### Now it is personal

Once the existence of the email chains became of general knowledge, these began to be addressed to the whole family. At first, Leonardo did not let them unanswered, especially when he felt there was the need to disprove false information, but once the conversation began to get more personal and even insulting, he decided to stop responding.

It was only a couple years later that Leonardo realized the reason of the long technical questions dictated to the minutes, when the four dissenters used the latter as proof to file a lawsuit against the company, alleging illegal accounting practices and requesting the impeachment of all the recent assemblies and the dismissal of the management. Even tough courts have dismissed all their claims, it was felt as a treason to the family, which, summed with all other aspects, burnt all bridges between both sides of the dispute.

## Hidden in the closet

Despite never being openly discussed, Leonardo suspected from asides that some problems emerged long ago. One of them was the old rumor amongst some of Fatima's and Gabriel's descendants claiming the original distribution of Alexander Rodrigues' shares had been inequitable. The problem was that Ignacio's branch had a bigger percentage than any other, and the fact it had fewer descendants even increased their imbalance feeling. To illustrate, some cousins had even claimed that the assembly voting process should be done by head rather than by percentage of shares. However, the facts remain that the original distribution had been done in nine equal parts as required by law, but subsequent deaths of Ignacio's brother and mother eventually left him with 3/9. Gabriel also held more because he bought his brother Cesar's participation, but all the other minor variations were exclusively due to later deaths and one-off transactions.

A further issue was linked to the second succession. The process was peaceful and consensual between men, but nonetheless had opened hidden irreparable breaches on the feminine side of the family. Actually, back then women did not have a say on the business but, in the typical Portuguese matriarchal family, their influence within doors could be immense. It goes back to when Gabriel, given his wife did not enjoy the yearly season on Quixote, instructed his younger daughter Sarah to be the matron of the farmhouse, a leading and prestigious position at the time. Sarah was helped by her single daughter, Teresa, who grew nurturing the ambition to succeed her. It happened however that, when Ignacio took the lead, he delegated the job to his daughter-in-law Alexandra. This angered Teresa, currently 83 years old, whose influence in her branch is said to be the main driver for the contestation against the three administrations since then.

Even though it seemed that nearly all the dissatisfied passive cousins who were represented by the dissenters came from this branch, what could Leonardo do if confidence was totally broken and they never even showed up to assemblies? For one side, any of his attempts to intervene and clarify had no credibility and had only worsened the conflict. On the other hand, how could he accede to the demands of those who had never even set foot on the premises? Or rather, to be honest, besides his resignation, after all this time he still did not know what the dissenters' intentions were.

## Setting the stage for the future

The management had been designing a complete strategy to cope with the problems both within the family and the business, which implied to update the centenarian bylaws.

**Soc. Alexander Rodrigues S.A.** – The first step was to convert the Private Limited Company into an unlisted Public Limited Company (*Sociedade Anónima*). This legal structure had several differences that made it more suitable to the current size of the family, whose younger generations did not even know each other. For instance, major changes, which were subject to approval by qualified majority voting, demanded only 2/3 of the shares present in assembly, instead of the current 75% of total equity. The goal was to simplify decision-making processes for future generations: if finding consensus (or even gather enough owners in assembly) was such an impossible task in those days, how would it be in the future? Yet, judging by last night emails, dissenters' adverse reaction, claiming that Ignacio's branch had the ulterior motive of opening equity to outsiders as to reduce others' shares and power, had awakened most of passive owners.

**Trading Company** – The current articles imposed many limitations to the management because it restricted company's activity to the sale of own-produced agricultural products. So, the second step would be the change the type of activity from agricultural to commercial, fundamental for the firm to diversify its activities with the two projects explained below. The goal was not only to reduce exposure to the cork market, but also to seek the so much needed scale advantages connected to turnover.

Namely, it would allow to create independent marketing, sales, and finance departments, and expand the workforce at all levels, including non-family managers in top-positions.

**Wine** – The firm was few steps away from being a renowned player in the industry: the producing team had great expertise, the brand had recognized quality, the history and seniority of the family represented a big plus in the market, and the internationalization campaign that Nicolas was making, besides being supported by communitarian funds, had granted an excellent distribution network. Growth was merely limited by the small productive capacity and this could only be worked around by purchasing grapes and wine for resale.

**Hotel** – With the help of specialist consultancy, the board had developed a five star hotel project to harness the idle estate in Lisbon. Tourism outlook was great, which combined with the unique conditions offered by the iconic historic building promised excellent financial results, not to mention the pride in owning one of the best hotels in town. Forecasts for the investment projected an internal rate of return of 10% and a net present value equivalent to six times the current annual revenues, and it did not even take into account the strong incentives and privileged financing conditions offered by the government. With the expected annual EBITDA of 1.4 million euro, the company could finally sustain losses in other business areas and probably even start to distribute dividends.

Leonardo expected such figures would finally please everyone, but it had not been welcomed at all by the usual wings. Arguing the family had no experience in tourism, they feared it would end up losing everything or, even worse, that they could have to pay it from their own pocket - a misunderstanding since it was not legally a possibility in Ltd.'s or S.A.'s.

## On the horns of a dilemma

Despite the burden in workload and expenses they caused, never dissenters had been a real obstacle to decision-making because they represented a minority. But now, for the first time, everything depended on them and they seemed determined to hold their cards.

Leonardo had already given up on convening the assembly to amend the articles of incorporation. Shareholders were not properly informed and prepared, and it was highly unlikely the needed 75% of approval were reached. He still believed it was an indispensable change but try it then would be too risky. After all, it would already be so hard to persuade all passive owners to come to a meeting that there could never be a second chance. But how could he raise awareness to the critical situation and motivate to the new business alternatives?

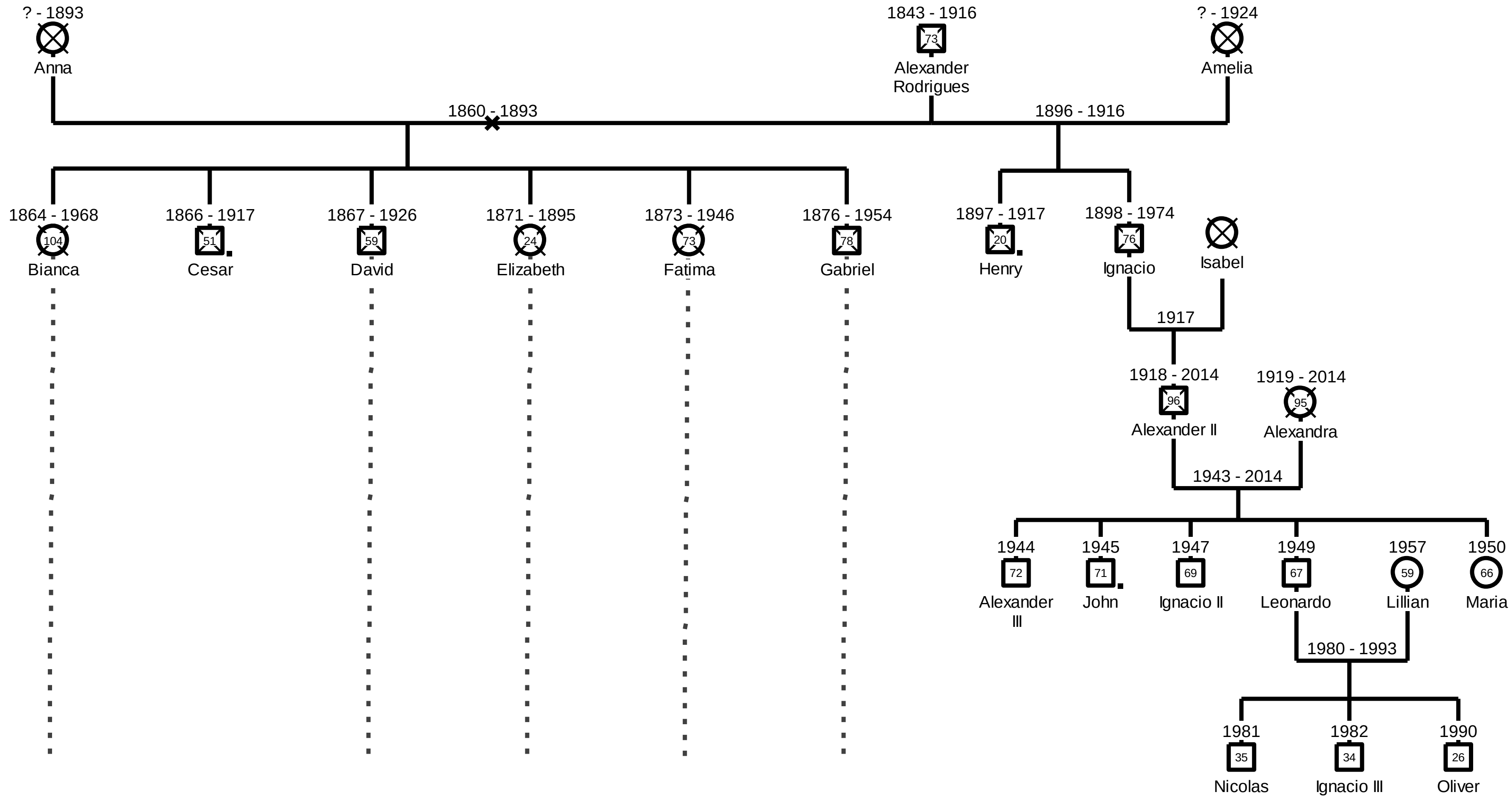
Should he consider the sale of the building and project to a third party as some dissenters preferred? Distributing part of the revenue may reduce their dissatisfaction and the remaining could be used to sustain the business a few more years while hoping for an unlikely recovery of the cork market. However, neither the management nor the majority of owners looked kindly to the loss of the historic building, together with 35% of its value in taxes, or the dividend distribution that, besides only giving a residual return per member, would jeopardize the company's future even more. And most of all, cash would serve little purpose without the change in by-laws because there was no other opportunities for investment and growth.

He even had weighted his resignation but, even though an external Board had the advantage of being free from the accumulated distrust to seek consensus, it could not parachute without any knowledge of the family and the business. Furthermore, the present situation was repellent even for a family run, let alone non-family managers, and the business dimension did not allow to pay for additional senior positions. Perhaps there could be a middle way, where an external consultant mediated a rapprochement between shareholders.

"Our founder risked everything he had to build this business at the age of 30. Nothing ventured, nothing gained, and in this case no comparison between what is lost by not trying and what is lost by not fully achieving the objectives." – Leonardo thought, resuming his walk – "None of us had to do absolutely anything to receive this legacy, so we don't have the right to drain it. Freely we have received, better we have to leave it."

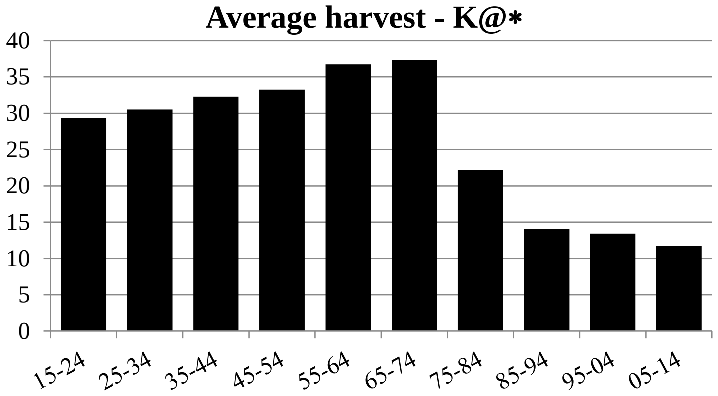
# APPENDIX

## Appendix 1 – Summarized genogram (selectively itemized) with share distribution by branches

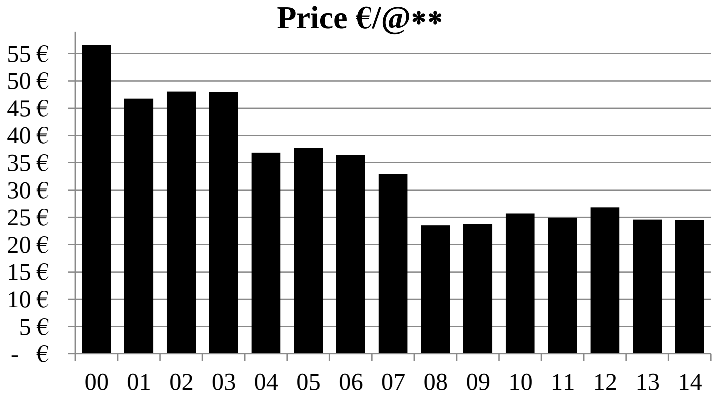



| Branch | B | C | D | E | F | G | H | I | TOTAL |
|---|---|---|---|---|---|---|---|---|---|
| Shares (%) | 8,1 | - | 4,8 | 8,9 | 15,1 | 25,9 | - | 37,2 | 100 |
| # Shareholders | 4 | - | 15 | 24 | 24 | 29 | - | 8 | 104 |
| # Living descendants | 13 | 0 | 57 | 64 | 102 | 109 | 0 | 34 | 379 |

## Appendix 2 – Cork's quantities and prices




* @ (arroba) is the traditional cork's measure: 1@ = 15 kg = 33 lb.



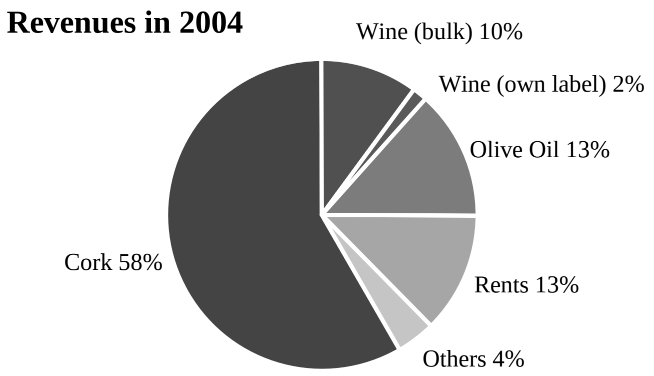

** All prices updated to inflation

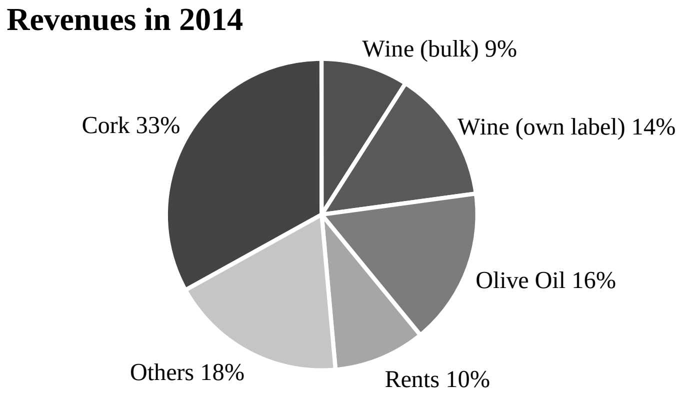
## Appendix 3 – Comparison of revenues per culture (2004* vs. 2014)

| Year | Cork | Wine (bulk) | Wine (own label) | Olive Oil | Rents | Others** | Total |
|---|---|---|---|---|---|---|---|
| **2004** | 583 K€ | 101 K€ | 15 K€ | 135 K€ | 125 K€ | 40 K€ | **1000 K€** |
| **2014** | 252 K€ | 69 K€ | 105 K€ | 124 K€ | 72 K€ | 140 K€ | **763 K€** |

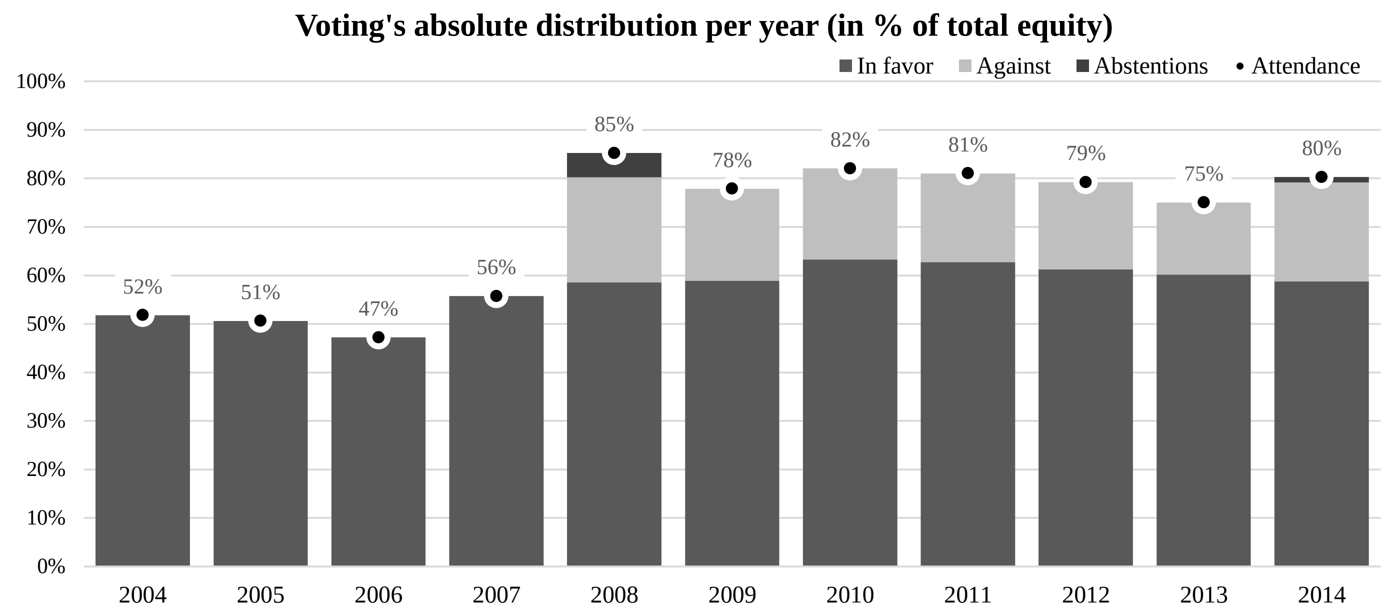
* 2004 values updated to inflation

** Includes subsidies, restaurant (closed for renovations in 2004) and extraordinary revenues




## Appendix 4 – Attendance and voting results for approval of annual report



# TEACHING NOTE

## Overview

(In the Abstract section)

During the purposed discussion, students are requested to do a critic analysis of the factors and multipliers that led to the tension between the shareholders, learn and apply the socioemotional wealth concept to characterize the current variety of opinions amongst them, and propose a reconciliation strategy based on their findings.

## Target Audience

This case was developed as a learning tool for Family Business courses of undergraduate and master programs in Management, with helpful examples and academic support to the learning of a varied collection of the most important concepts in this field, such as: the cousin consortium specificities; active vs. inactive and majority vs. minority owners' conflicts; socioemotional wealth; family governance structures (family meetings, council, and protocol); and fair process. In order to take full advantage of the discussion, students, or at least their instructor, should have basic familiarity with the concepts of stewardship, agency theory, genograms, zero-sum dynamics, and the three circles model of system theory.

## Learning Objectives

This teaching note presents a suggested analysis, discussion, and resolution of the case, as well as the needed underlying theory, to allow students to:

1. Understand the increased complexity and specificities of relational conflicts in business families in later stages, and identify their original causes and future consequences.

2. Be aware of the weight of the different dimensions of socioemotional wealth in family owners, and how they can affect differently each one's criteria.

3. Know and properly apply the main mechanisms for the prevention and solving of conflicts in business families.

## Suggested Questions

### 1 – Problems from the past

**1.1 - What seem to be the most determinant factors to the long lasting hostile relationship between shareholders?**

Students should be able to identify, from the "Hidden in the closet" section, the share distribution and second succession to power as the original trigger of the dispute. By analyzing the extensive list of problems contested, students may perceive that these invariably come from the deterred branch (G) towards the one more involved in the management of the firm (I). Alienation from power and perceived unfairness are common reasons of anger and frustration between family owners that generate hard to solve conflicts (Poza 2007, 45), in this case both role conflicts - against management - and affective ones - against branch I - (Chandler 2015, 1306). To check for reading and assure proper understanding by the whole class, the instructor may conduct, step-by-step on the chalkboard, a redrawing of the genogram based on pupil explanation of the events, starting with the one presented in Appendix 1 until it matches the one in Appendix 5.

**1.2 – Why do these incidents still affect the family dynamics at present?**

Since the referred succession, the family developed from the sibling generation (6 siblings) to a complex cousin consortium (more than 100 members), with ownership spread over different generations and branches, but none with enough voting shares to control decisions – recall Appendix 1 (Gersick et al. 1997, 47). In fact, siblings' career choices tend to influence the cousin presence in management, perpetuating discrepancies and reducing general commitment to the company: while one branch becomes dominant, the others begin to step back from involvement (Gersick et al. 1997, 50). Therefore, and given that share dilution through generations decreased economic interest (Mcclure 2014), most shareholders outside the management branch became low involvement supporters or merely passive owners. However, as conflicts were also transmitted through generations and polarize branches into camps (Gersick et al. 1997, 50), most descendants from the deterred branch kept reacting hostilely.

**1.3 – Regarding the management and dissenters' behaviors along the way: how did they worsen the conflict? Why did they react like that?**

Regarding the management behavior, students are expected to mention both the lack of dividend distribution or redemption policy, and the inadequate information and lack of inclusion of other branches in the company's activities. In fact, continued lack of liquidity, which implies an altruistic expectation of return from owners, is hard to take for inactive members. They will only accept it if there is a trade-off for plenty opportunities to receive privileged information and education, in a mutual affection and influence relationship between active and inactive members, in order to engage with the family values of stewardship. (Poza 2007, 31)

For their part, dissenters exacerbated the problem by reacting aggressively: instead of seeking enlightenment near the board, they went straight to public courts and organized undercover meetings and email chains between carefully selected shareholders. Responsible ownership in a cousin consortium requires one to contribute to cohesiveness of the family and seek education about the business on his own (Aronoff and Ward 2002, 20), as well as "a public posture of loyalty and support, a willingness to think broadly about the common financial needs, and a willingness to contribute in some appropriate way one's talent, effort and opinions." (Gersick et al. 1997, 52).

While both conducts were clearly inappropriate, no lesser were they expectable. In fact, family managers often consider that shareholders do not deserve to be involved in the decision making until they self-educate in financial and operational matters (Mcclure 2014), fearing the outcome of such uninformed democratic decisions (Poza 2007, 41). Nevertheless, majority branches are still more open to dialogue than family members with reduced power, who commonly interact with negative affect, through threats and punishment, and with more inhibited social behavior (Chandler 2015). The former see themselves as stewards seeking the common interest, whereas the latter deal with management through a principal-agent relationship (Madison et al. 2016). Therefore, minority owners, when made to feel impotent, can sue the company and take problems public as a way to still exercise their power (Aronoff and Ward 2002, 57).

Finally, the keenest students may also identify that this Board is the first in later generations that does not include any member of the G branch, which escalates this branch's feeling of being shut out of the decision process (Gersick et al. 1997, 52).

**1.4 – Taking the discussed conflict into consideration, how propitious seem the current circumstances to raise the discussion about the suggested changes? Why?**

The question is intended to focus on the need and urge to discuss the diversification investments and review of the governance structure - to which students should be able to find arguments in both ways - rather than to analyze their financial attractiveness, for which, for the sake of the case, the prospects of the management are taken as trustworthy in all questions.

On one hand, these times may well be the last opportunity to fit the company's legal and governance structures to its shareholder particularities, while they still know each other. Once the next generation steps in, the exponential dispersion of shares, which reflects in decreased engagement and poses a threat to continuity (Mcclure 2014), can make the gathering of an assembly quorum a virtually impossible aspiration, not to mention achieving agreement over structural questions. Moreover, the current conflict in the family can represent an opportunity to help it to properly differentiate between the two different systems on their bases - the family and the business ones – and thus generate more competitive advantage (García, Castejón, and Perez 2014). In fact, higher professionalization of family businesses often comes when family members recognize the need of supplementary skills and governance techniques in moments of significant growth (Dyer 2010), as the proposed investments. Finally, the sustainability of the company seems to be at stake, and waiting for better conditions could make it lose the right timing to invest.

On the other hand, one cannot ignore the serious downsides caused by the relationship between the supporters and dissenters, compounded by the court proceedings, and by the current economic conditions of the company. As seen in the case, conflict has already become personal, and this sort of relationship problems are highly detrimental to work groups, as they encourage withdrawal from the table even before the negotiating starts (Jehn 1995). Students familiar with the concept, can be able to identify the zero-sum dynamic in their relationship. This dynamic refers to relationships marked by a direct trade between one side's perceived gain and the other's perceived loss, common and critical when "those active in top management agree on a growth strategy, family members employed elsewhere believe that, in settling for greater reinvestment in the business, they will have to accept reduced distributions to shareholders" (Poza 2007, 32). Worse still, zero-sum dynamics are exacerbated in the absence of growth: when the pie does not get any larger, members start fighting for the size of their slice. This makes members seek only their individual interests, blame others for downturns, and minimize personal risk instead of maximize business gains. Under these circumstances, even "promising alternatives for growth may be rejected as competition and in-fighting for resources – and for right or might – spread" (Poza 2007, 172), as verified in this case.

## 2 – Current hindrances

**2.1 – The suggested project of diversification (wines and tourism) seems very promising, with considerably high financial estimates that portend the resurgence of dividends. In a common company, this "enlargement of the pie" should be enough to gather shareholders under the same flag again. Why is it not happening here?**

Over the past decade, academia has been prolific in the study of family firms' unique particularities that make them considerably less driven by the financial criteria followed by the remaining companies, which could not be explained by the traditional agency and resourced based view theories (Dawson and Mussolino 2014). Starting from the behavioral agency theory, by which decision makers follow a loss avoidance logic (Gottardo and Moisello 2015), Gómez-Mejía et al (2007) were the first to introduce the concept of Socioemotional Wealth (commonly referred as SEW), referring to the sum of nonpecuniary benefits and affective endowments that family owners strive to derive from the business. Currently, this is scholarly accepted as the key point of difference between family companies and other types of businesses, since the former seem to be managed in order to preserve SEW, even at the expense of financial gains (Debicki et al. 2016), which is not to say these are fully ignored (Gómez-Mejía et al. 2011). More specifically, this concept characterizes the family members' desires for power of influence and decision, dynastic continuity, perpetuation of family values, pride of identity and legacy, social reputation and recognition for generosity, sense of belonging, and opportunities for altruism towards the family (Gómez-Mejía et al. 2007; Pascual Berrone et al. 2010; Gómez-Mejía et al. 2011; P. Berrone, Cruz, and Gomez-Mejia 2012; Deephouse and Jaskiewicz 2013; Hauswald and Hack 2013; Mullins and Schoar 2013; Martin, Campbell, and Gómez-Mejía 2014; Miller and Le Breton-Miller 2014; Morgan and Gómez-Mejía 2014; Vardaman and Gondo 2014; Gottardo and Moisello 2015; Debicki et al. 2016).

**2.2 – After reading the "The bind that ties", which of the described patterns do you identify in this company?**

In order to consolidate the learning of the SEW concept and how it affects the present case, students should be requested a group assignment, which is explained below in the "Teaching Plan" section. All students should be advised to read the introduction and conclusion sections of the referred paper, while regarding the remaining content, they can be split into 6 different groups (to reduce workload, foster widespread participation, and facilitate assessment). The expected results are presented, according to the suggested division, in Appendix 6.

**2.3 – Even so, should we not expect to see the shareholders aligned in their interests, being them financial or socioemotional?**

No, actually the notion that families are naturally aligned in their interests is a misconception. Quite the opposite, heterogeneity and conflict of interests between branches are increasingly common with the rise in number of elements (Chandler 2015), making even some cousin consortiums function as multifamily firms (Steier, Chrisman, and Chua 2015). In this case, besides the conflicts, members seem to attribute different weights to the different components of socioemotional wealth. For instance, one can imagine how reputation in the wine production market rewards more the management than shareholders from other professional areas. In this sense, students may notice that the meetings organized by dissenters took place in another town because they live far away from the business, which is tendentially related with lower attachment to the real estate and the local status that the company owns (Gersick et al. 1997, 50). Furthermore, the CEO admits he cannot know nor understand the dissenters' intentions, while also complaining they seem to have no clue and interest about the business. This mutual lack of understanding of each other's feelings and intentions denounces an unhealthy culture where information does not flow properly, which may explain the absence of a common vision (Poza 2007, 27) regarding, for instance, the importance of continuity, dividends, growth, reputation, perks to the family, or altruism towards community. Indeed, the fear of losing value in patrimony (through seizure), benefits (usage of the residence) and power (possibility of equity issue) were some of the arguments used by dissenters to foster mistrust against the management, especially regarding the management's new strategy.

**2.4 – From all the observed influences of SEW that can be affecting shareholders differently, which one seems more preponderant in this situation?**

After having thoroughly followed their peers' presentations, students should be able to identify the different attitudes towards risk as the main learning to consider to the solving of this case. As a matter of fact, the family seems to have a risk-averse behavior, patent in its business model stability, with no debt or new ventures. Congruently, the only large investment through debt referred in the case, the building of the two dams, was one of the events that prompted strife in the past. However, with the continuity of the firm under threat due to the declining performance, management and its supporters prefer to start a new venture instead of losing control of the iconic building owned since the very beginning of the company, even at the cost of increased risk (Fernando, Schneible, and Suh 2013). From their long-term perspective, they appreciate that, by holding two diversified businesses, the company can benefit from risk-reducing effects through fund transfers between them (Steier, Chrisman, and Chua 2015). On their hand, minority shareholders typically fear to see their value expropriated by majority blocks and therefore prefer to capture immediate liquidity, while the latter have greater benefits from seeking firm continuity and growth because they see it as an asset to leave to their descendants (Anderson and Reeb 2003).

## 3 – Which resolution and reconciliation paths to the discussed problems could you advise to the management and/or shareholders group?

**1st – Provide education that enables participation**

As seen before, the family has been suffering the negative effects of the growing estrangement of some shareholders from the company and, since keeping shareholders informed and engaged with the business is a mutual responsibility, they should be invited to tackle these problems as a whole in family meetings (Poza 2007, 45). Nonetheless, in cases with such large families, it is more effective to carefully pick a smaller set of influential elements who can positively represent and head the entire family than to aim to widespread democratic participation, which leads to the creation of family councils (Mcclure 2014). This governance body, equivalent in family to the board on the company, is an institutionalized form to periodically hold family meetings, and should be responsible to coordinate communication and education, enable conflict solving, and stimulate participation in policy-making (Poza 2007, 277). However, as the management claims, most shareholders do not have the knowledge required to effective decision making (e.g. never visited the premises and request for voting by head rather than by shares). Therefore, before they develop into planning and decision-making bodies, these meetings should start by being educational events about the state of the business, financial matters, the strategy followed, and the challenges it faces, as well as the rights and duties of a shareholder (Poza 2007, 39, 41). Education about the business and its forms of governance is critical to prevent abdication of control, because it helps to understand the risks of inaction (softening resistance to change), provides a common language and framing of its problems (enhancing the quality of contributions), and offers several new mind-opening possibilities to the business (renewing hope and stimulating excitement and commitment) (Lansberg and Gersick 2015).

**2nd – Allow for participation that prevents future conflict**

Fighting the zero-sum environment is the most common reason that makes business families hold meetings and create a council (Poza 2007, 39) but these, by themselves, have no proof of positive influence in family conflicts if not accompanied by a family protocol (García, Castejón, and Perez 2014). A family protocol or constitution is a formal but non-legal "document that summarizes the family's mission, its fundamental values, the functions and responsibilities of each governance body (e.g., Board, Family Council, Family Office) and each policy (e.g., employment, conflict of interest, dividend, retirement) that the family owners have adopted to regulate their relationships with each other, their business, their philanthropy, and their collectively owned assets."(Lansberg and Gersick 2015).

Both the vision, that sets what the family wants its company for, and the policies, that aim to address typical issues beforehand, ought to represent the whole family preferences and so must be the result of a widespread participation rather than decisions enforced by the family council or, even worst, by the board (Eckrich and Mcclure 2013). The concept of fairness in family business is perceived through different criteria (equality, equity/merit, or needs) used to distribute the outcomes (distributive justice) according to the perspective of each sub-system (ownership, business, family, respectively) (Baldridge and Schulze 1999). Due to the blurred boundaries between these sub-systems, and even though it takes longer, it is essential to place the effort on an inclusive process that gives voice to everyone - procedural justice - instead, because it allows members to understand and accept decisions even when these do not favor them, and eliminates the apparent negative tradeoff between emotional and economic performance (Fair Process: Van der Heyden, Blondel, and Carlock 2005).

As a matter of fact, due to the entrenched distrust between both sides, the family should consider resorting to an outside advisor to mediate this discussion and help the launching of the family council, bringing to family members a perception of fairness and objectivity in the process (Poza 2007, 276), because mediators commit to the process rather than to an option, and prevent discussions from becoming personal (Russo and Schoemaker 2002, 181).

At this point, students should recall important matters to be discussed, as the (false) inequitable distribution of shares in the second generation or the possibility of inclusion of an element from branch G in the Board. Likewise, other forms of shareholder engagement could also be suggested. When the management foments them to visit the premises, interact with employees and stakeholders, and participate in auxiliary governance activities, it helps both the relationship (increasing trust, comprehension of sacrifices needed, and sense of responsibility to contribute) and the firm’s performance (through informed decisions and value-added contributions) (Mcclure 2014).

### 3rd – Hard measures

Sometimes, conflict escalates to a point where achieving consensus could take so long that the discussion would backfire (Russo and Schoemaker 2002, 182), making the buyout of the outsiders becomes more realistic than to aspire to reach cohesiveness again (Aronoff and Ward 2002, 54). Even though the firms does not have enough liquidity to redeem them, keeping disagreeing cousins captive can prove far more costly in terms of time, emotional stress, and legal fees (Gersick et al. 1997, 53). The solution may be the creation of redemption mechanisms, based on specialized external evaluation of shareholdings to increase trustfulness, with policies that specify the circumstances under which transactions can occur (e.g., frequency, percentage of profits set aside to redemption pool, use of internal broker) to minimize unfairness and negative effects on the company (Aronoff and Ward 2002, 49; Mcclure 2014, 53). Actually, even when not exercised, the simple ability to sell their stock is often enough to appease dissatisfied owners, who tend to recommit to ownership with renewed enthusiasm (Poza 2007, 60).

## What Happened

The case has not yet been solved. The Board ended up deciding to hire a family business consultant to mediate the wording of a family constitution and the creation of a family council. Despite his efforts, consensus was not achieved and, therefore, only 66% of the shares committed to the outcomes. Branch G and part of branch F made a parallel commitment (30% of shares) to block any changes in bylaws and chose three members to represent them near the Board, whilst the remaining 4% belong to other passive owners who chose to ignore this process. The current family council has six elected members, only one from branch I, and is considering to invite the above referred representatives to occupy the three vacant seats. According to the consultant, the three main claims from dissenters were: displeasure with the lack of information from the management, fear of losing wealth through indebtedness, and refuse to forego their blocking power with 25%. In 2015, the firm returned to (a small) profit thanks to wine sales, which continued to grow above expectations (+25%).

## Teaching Plan

This case was divided in three parts (45 min) to be discussed in separate classes, in order to allow the instructor to use the remaining class time to deepen the theoretical concepts introduced by it. Alternatively, the last two parts can be discussed within the same lesson. At the end of the first part, students should be split into 6 groups and be assigned a section (according to the division patent in the Appendix 6) of the article "The Bind That Ties" by Gómez-Mejía et al. Each group should then summarize their corresponding content and how it reflects on the case, and present it to their colleagues in no more than 4/5 minutes at the beginning of class two. The suggested time planning is presented below:

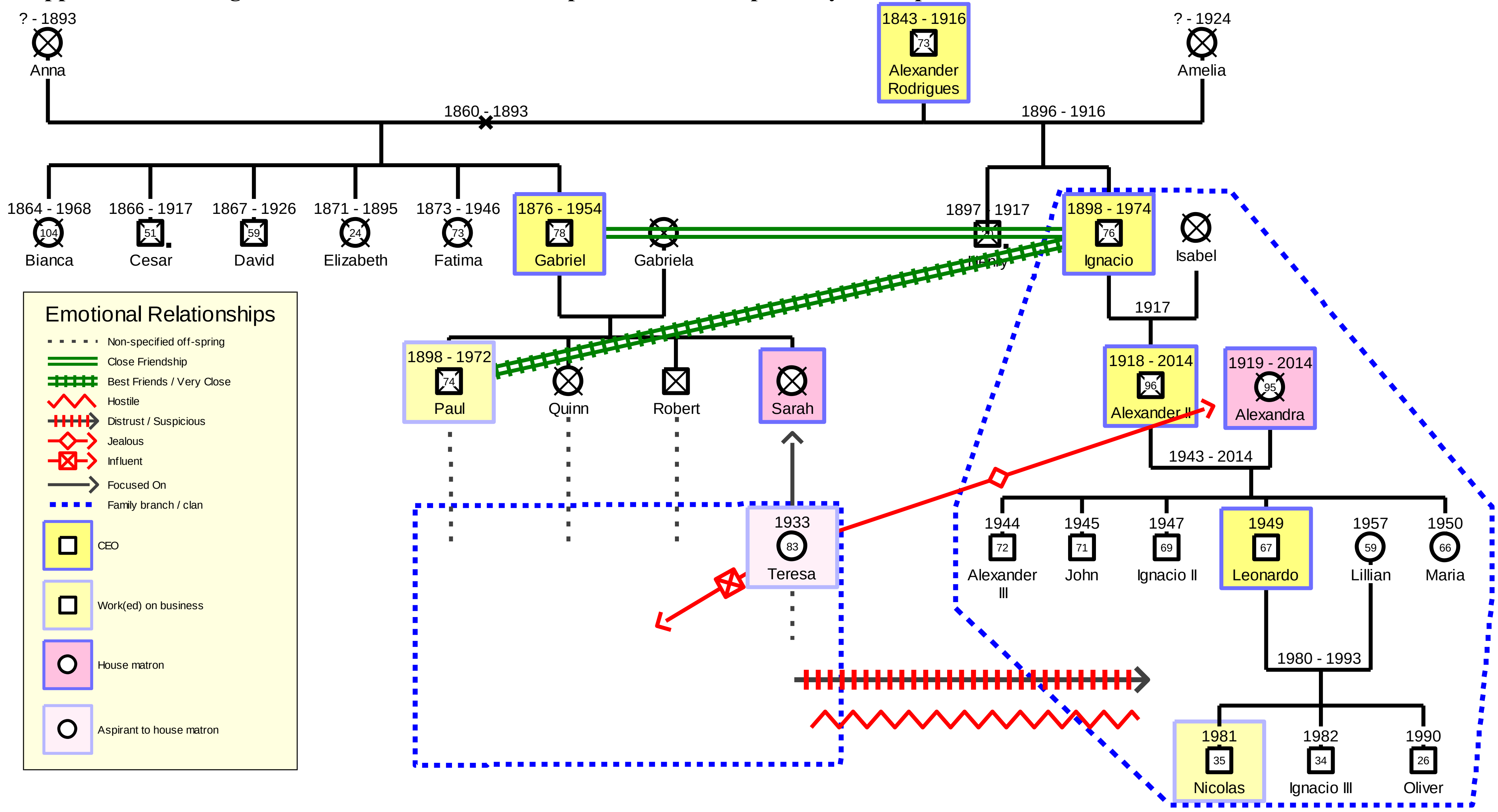
| Part | When | What | Duration | |
|---|---|---|---|---|
| 1 | Class 1 | Case introduction by instructor and/or volunteers | 5 min | 45min |
| | | Discussion of questions 1 | 30 min | |
| | | Question 2.1 and launch of group assignment | 10 min | |
| Homework | | Suggested assignment | 2 hours | |
| 2 | Class 2 | Group presentations – question 2.2 | 6x5=30min | 45min |
| | | Discussion of results with questions 2.3 and 2.4 | 15 min | |
| 3 | Class 2 or 3 | Discussion of question 3 | 30 | 45min |
| | | Instructor wrap-up and "what actually happened" | 15 | |

## Background Reading

The following list can be used both by the instructor and his pupils to prepare or deepen the contents taught in this case:

- Poza 2007 – Comprehensive support book, covering all topics except SEW.
- Question 1: Gersick et al. 1997 – The development model of family business, with the three sub-systems' and ownership stages' particularities
- Question 2: Gómez-Mejía et al. 2011 – Thorough collection of academic studies about SEW's effects on family businesses' decisions (shall be given to students)
- Question 3: Aronoff and Ward 2002 – Ownership rights, duties, and conflict solving + Van der Heyden, Blondel, and Carlock 2005 – Deepens the concept of Fair Process.

**Appendix 5 – Genogram with emotional relationships and branch G partially developed.**



## Appendix 6 – Expected Results from Student's Assignment

| Typical SEW patterns described in the paper | Application to the case |
|---|---|
| **Management Processes** | |
| **Succession**: Desire to transfer business control to next generation. Favor a successor from within the family. Prepare successor through personal mentoring with leader. | The successor, current leader's son, is already chosen and being prepared through co-working with the latter. In this case, the CEO's "reluctance to plan for his succession" does not apply. |
| **Professionalization**: Lower to avoid decrease family control, but also due to smaller size and fewer resources. | CEO's claims the firm does not have resources to hire more people and that an outsider successor is out of question. Still, the number of non-family qualified workers has been increasing and the proposed strategy contemplates hiring of outside talent, even for the board. |
| **Human resource management practices**: Informal systems of communication with employees. Selection based on candidates who share family values. | Indiscriminate monetary compensation. Close and loyal relationship with employees. |
| **Strategic Choices** (from Risk Taking to International Diversification) | |
| **Risk Taking, Corporate** and **International diversification**: Risk-averse under normal conditions, but risk-willing to prevent losses to accumulated endowment, namely when performance is below target, in order to retain family control. Therefore, they diversify less (because it requires external funding, talent from outside the family and changes in the organization) unless there is a strong fear-factor due to high systematic and unsystematic risk and declining performance.<br>Also, they tend to be less internationalized, even though it reduces systematic and unsystematic risk, because it demands external funding and expertise. | Historically, only during economic downturns did the family seek diversification strategies with increased risk: fruit sale (new business), and wine and tourism business (which demand both debt, outside talent, and a whole new form of governance and firm structure).<br>Dams were only built under extremely favorable conditions, with governmental support through debt.<br>The company seek internationalization in recent years, to grow the wine business, but it was also done with communitarian funds and by developing in-house expertise. |
| **Debt**: is avoided, at least when its acquisition may exacerbate the possibility of family conflict. | Investments that entail debt (dams and hotel) were highly contested, and firm tends to have zero debt. |
| **Strategic Choices** (from Acquisition behavior to R&D) | |
| **Acquisition behavior, Accounting choices, R&D** | These are not reflected by data presented in the case. |
| **Organizational Governance** | |
| **Role of the Board, Incentive alignment,** and **Agency Contract** | These are not reflected by data presented in the case, but students may note that never was a CEO dismissed by the family. |
| **Stakeholder Relationships** | |
| Concerned about family reputation and thus more responsive to claims and sanctions that stigmatize them as an irresponsible corporate citizen. Tend to create and protect long-term relationships. | The court case and its public repercussions were the trigger to contestation in the present generation.<br>The company opts for long-lasting commercial partnerships with small retailers and distributors for the wine and olive oil businesses. |
| **CSR**: More environmentally friendly and socially responsible behaviors, mostly when socially and geographically embedded at the local level. | The family has a long historic record of social altruism, mostly in the farm region, and is particularly environmentally conscious (organic and biodynamic production) |
| **Business Venturing and Contingency Variables** | |
| **New ventures and entrepreneurship**: as the business matures, families are more likely to build portfolios of related businesses, meaning that new ventures are restricted to core-related activities. | The hotel project is the first completely new venture considered by the family. Yet, the development strategy of the restaurant, fruit, and wine businesses can also be analyzed under this trend. |
| **Contingency Variables**: While firm moves through generations, sew weight lessens and financial considerations start become more important. This happens with the dispersion of shares, when family unity is weakened. Also, families are more willing to make economically driven decisions under performance and external hazards. | These contingency variables have different effects in both sides of the discussion, which illustrates the loss of family unity:<br>Some shareholders request for dividends and want to sell the urban estate, because they are less influenced by SEW than others. Same thing that happened after the revolution.<br>Management and its supporters, as already seen before, have more tolerance to risk, diversification, and debt when hazard threatens their SEW. |

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